No. 14901

In the United States Court of Appeals for the Ninth Circuit

JOHN PIERCE, PETITIONER

v.

SECURITIES AND EXCHANGE COMMISSION, RESPONDENT

PETITION TO REVIEW AN ORDER OF THE SECURITIES AND EXCHANGE COMMISSION

BRIEF FOR RESPONDENT

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CITATIONS

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NATURE OF APPEAL

Petitioner, John Pierce, seeks to have this Court set aside an order of the Securities and Exchange Commission (the "Commission") denying him registration under Section 15 (b) of the Securities Exchange Act of 1934 (the "1934 Act"), 15 U. S. C. § 78*o* (b),[1] and the right to do business (other than an exclusively intrastate business) as a broker and dealer in securities. The Commission found that

[1] The provisions of the Securities Act of 1933 and the Securities Exchange Act of 1934, and the Commission's rules and regulations thereunder, involved herein are set forth in the Appendix, pp. 33–38, *infra*.

petitioner's course of conduct prior to his application for registration was such that it would be contrary to the public interest to permit him to engage in the securities business with members of the public, including permission to act as a broker handling the accounts of others. Petitioner now seeks from this Court the authorization which the Commission denied him.

JURISDICTION

The Commission's order was entered on August 16, 1955 (R. 250.10).[2] The petition for review was filed on October 14, 1955 (R. 247). Petitioner resides in Las Vegas, Nevada (R. 210). This Court has jurisdiction to review the Commission's order under Section 25 (a) of the 1934 Act, 15 U. S. C. § 78y (a).

COUNTERSTATEMENT OF THE CASE

Section 15 (a) of the 1934 Act, 15 U. S. C. § 78*o* (a), requires prior registration with the Commission of everyone who acts as a broker or dealer in securities (other than in an exclusively intrastate business or with respect to certain exempted securities not involved here) and who uses the mails or instrumentalities of interstate commerce in his transactions. Reg-

[2] "R." refers to the two volumes of the Transcript of Record, the first of which is printed. The second volume consists of the multilithed Recommended Decision of the Hearing Examiner and the Commission's Findings, Opinions and Orders. These multilithed documents are referred to by the transcript record page number of each document followed by a period and then the original number of the particular page involved. Thus, page 10 of the Commission's Findings, Opinion, and Order of August 16, 1955, contained in Volume II of the Transcript of Record, is referred to as R. 250.10.

istration is achieved through an application filed with the Commission pursuant to Section 15 (b) of that Act, 15 U. S. C. § 78*o* (b), which becomes effective after a short period of time unless the Commission, after notice and opportunity for hearing, orders that the application be denied for reasons set forth in that subsection. Section 15 (b) requires denial of registration, *inter alia,* if the Commission finds that the applicant has wilfully made false or misleading statements in his application with respect to any material fact or has been temporarily or permanently enjoined by any competent court from engaging in practices connected with the purchase or sale of any security, or has wilfully violated any provision of the Securities Act of 1933 or the Securities Exchange Act of 1934, or any rule or regulation thereunder, and finds that denial is in the public interest.

It is not disputed that for three years prior to the filing of the instant application petitioner engaged in business as a securities broker and dealer in violation of Section 15 (a) of the 1934 Act. Both the Hearing Examiner and the Commission found that these violations were wilful, and petitioner does not challenge those findings.

During that period petitioner was warned several times by Mr. Charles R. Burr, Assistant Regional Administrator in charge of the Commission's Los Angeles Branch Office, that he was violating the 1934 Act and was advised to file an application for registration if he desired to continue in business as a securities broker and dealer (R. 137–142). Petitioner, however, represented to Mr. Burr, and falsely so,

that he was trading for his own account only, and that he was not engaged in business as a broker or dealer (R. 139).

On May 7, 1954, petitioner finally filed an application for registration (CX 30, Tr. Doc. 64).[3] Thereafter, in June of 1954, the Commission instituted proceedings to determine whether petitioner should be permitted to be registered. On the day before the scheduled hearing, August 3, 1954, petitioner withdrew his application (R. 221–2). It appears that even while this application was pending, and thereafter, petitioner continued to act as a securities broker-dealer in violation of the 1934 Act. (See CX 9, 22–27, Tr. Docs. 43, 56–61.)

On October 7, 1954, the Commission instituted an action in the United States District Court for the District of Nevada to enjoin petitioner from continuing to engage as a securities broker and dealer in violation of Section 15 of the 1934 Act. *S. E. C.* v. *Pierce,* D. Nev., Civil Action No. 70.[4] Thereafter, on October 28, 1954, defendant filed the instant application for registration, and resisted the entry of any injunctive order on the ground, *inter alia,* that such injunction would be prejudicial to his applica-

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[3] The reference is to the Commission's Exhibit included in its Certificate of Transcript of Record, and to the transcript document number assigned thereto.

[4] It appears also that previously, on August 18, 1953, the California Commissioner of Corporations had issued a "Desist and Refrain Order" against Pierce for engaging in business as a broker and dealer without being licensed to do so, in violation of the state Corporations Code. See Exhibit 1 to Burr affidavit of October 4, 1954, in the above action.

tion before the Commission. (Defendant's Answer, filed Nov. 12, 1954.) No injunction has been issued in that action; for on September 23, 1955, a stipulation was entered into, and approved by the court, to the effect that the Commission's motion for a preliminary injunction would be removed from the calendar with the understanding that the court would entertain and grant a motion for a permanent injunction during that time if Pierce engaged in any further violation of Section 15 of the Act. The stipulation provided also that after nine months the District Judge would entertain a motion to dismiss the action if said motion were supported by Pierce's affidavit that he had not engaged in any violations of Section 15 during that period. The nine months' period recently expired. At this writing no motion has been filed.[5]

As previously noted, the instant application was filed shortly after the institution of the Commission's action for an injunction (R. 7, 9). On November 5, 1954, the Commission instituted proceedings pursuant to Section 15 (b) of the 1934 Act to determine whether the application should be permitted to become effective or should be denied (R. 9). In addition to the aforementioned violations of the registration requirements of Section 15 (a) of the 1934 Act, the Order for Proceedings referred to information reported by the Commission's staff to the effect that

[5] These facts of official record have relevance, *inter alia*, to petitioner's assertion that he was "unmolested" until, acting on the advice of counsel, he decided to "regularize" his activities and register, and that, having done the right thing, he has now had "the book thrown at him" (R. 36).

Pierce had been fraudulent and deceitful in his transactions with and on behalf of customers in violation of Section 17 (a) of the Securities Act of 1933 (the "1933 Act"), 15 U. S. C. § 77q (a), Section 10 (b) of the 1934 Act and Rule X–10B–5 thereunder, 15 U. S. C. § 78j (b), 17 C. F. R. § 240.10b–5, and Section 15 (c) (1) of the 1934 Act and Rule X–15C1–2 thereunder, 15 U. S. C. § 78*o* (c) (1), 17 C. F. R. § 240.15c1–2, and that the financial statement contained in his application for registration was false and misleading in violation of Section 15 (b) of the 1934 Act and Rule X–15B–8 thereunder, 15 U. S. C. § 78*o* (b), 17 C. F. R. § 240.15b–8 (R. 9–21).

Hearings were held before Edward C. Johnson, the Hearing Examiner designated in the Commission's Order, in Los Angeles, California, in November and December of 1954. On November 26, 1954, Pierce consented to postponement of the effectiveness of registration pending final determination of the question of denial. By order dated November 29, 1954, the Commission accepted his consent (R. 249.2, 249.4).

On February 8, 1955, the Hearing Examiner filed his Recommended Decision (R. 249). He found, and noted that Pierce himself had conceded, that from August of 1951 until October of 1954 Pierce had done business as a securities broker and dealer without registration in wilful violation of the 1934 Act. He found, however, no violations of the anti-fraud provisions of Section 17 (a) of the 1933 Act, and Sections 10 (b) and 15 (c) (1) of the 1934 Act, and Rules X–10B–5 and X–15C1–2 thereunder (R. 249.11–249.32). The financial statement, in his opinion, was

inaccurate in understating Pierce's unsecured liabilities; but he did not believe that there was sufficient evidence of a wilful violation of Section 15 (b) and Rule X–15B–8 (R. 249.32–249.39). He concluded that the public interest did not require denial of registration, observing that Pierce had been "forthright" in his testimony, had "learned the errors of his ways," had suffered enough from the cost and duration of the proceedings and the postponement of registration, and that in the circumstances no "additional penalty" was warranted (R. 249.16, 249.42–249.44).

The Commission's Division of Trading and Exchanges filed extensive exceptions to the Hearing Examiner's Recommended Decision (Tr. Docs. 24, 25). In response, Pierce's counsel declined to answer particular exceptions and arguments of the staff, requested adoption of the Recommended Decision, and objected to any review of the findings of the Hearing Examiner (Tr. Doc. 27). Moreover, his counsel did not seek oral argument before the Commission (R. 251.3).

The Commission made an independent review of the record, and on August 16, 1955, issued its Findings, Opinion and Order denying Pierce's application for registration (R. 250). The Commission found that Pierce not only had wilfully violated Section 15(a) of the 1934 Act in doing business as a broker and dealer in hundreds of transactions during a period of several years immediately preceding his application without being registered, but had also wilfully violated the previously mentioned anti-fraud

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provisions of the 1933 and 1934 Acts in his dealings with a customer. It found further that his omission to disclose substantial liabilities in the financial statement in his application was also wilful and rendered that statement materially false and misleading. The Commission concluded that the public interest required denial of the application.

Thereafter, Pierce sought and obtained an extension of time beyond the normal five day period in which to file a petition for rehearing [6] (Tr. Docs. 29–31). That petition was not filed until September 26, 1955 (R. 22–37).

On October 14, 1955, while the petition for rehearing was still pending before the Commission, Pierce filed the instant petition for review of the Commission's order of August 16, 1955. Thereafter, on October 24, 1955, the Commission filed its Memorandum Opinion and Order denying the petition for rehearing (R. 251).

ARGUMENT

Preliminary Statement

The proceedings before the Commission involved petitioner's fitness to do business as a broker and dealer in securities on behalf of and with members of the investing public. The nature of the securities business is such that, as a practical matter, the average customer must and generally does place great

[6] Rule XII (e) of the Commission's Rules of Practice, 17 C. F. R. § 201.12 (e).

reliance upon the honesty and integrity of the broker-dealer with whom he does business. Securities are not ordinary commodities—such as food or clothing—whose value the average customer may be in a position to appraise fairly accurately. Rather, in the words of Congress, securities are in a very real sense "intricate merchandise."[7] The business of trading in them "is one in which opportunities for dishonesty are of constant recurrence and ever present.[8] The business was "considered one peculiarly in need of regulation for the protection of the investor."[9] The state "blue sky laws" having been regarded as inadequate, federal regulation was provided.[10]

This case involves an important aspect of the federal regulation—namely, the registration or licensing of persons who desire to engage in the securities business (other than in an exclusively intrastate business) and who use the mails or instrumentalities of interstate commerce in their transactions. (Section 15 (a) of the 1934 Act.) Responsibility is placed upon the Commission to see to it that persons who have been guilty of specified derelictions reflecting adversely upon their integrity and fitness to engage in the securities business are not authorized to do so where such would

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[7] H. R. Rep. No. 85, 73d Cong., 1st Sess. (1933), p. 8.

[8] *Archer* v. *SEC*, 133 F. 2d 795, 803 (C. A. 8, 1943), *cert. denied*, 319 U. S. 767 (1943).

[9] *Charles Hughes & Co., Inc.* v. *SEC*, 139 F. 2d 434, 437 (C. A. 2, 1943), *cert. denied*, 321 U. S. 786 (1944).

[10] *Ibid.*

be contrary to the public interest. (See Section 15 (b).) Among the specified grounds for denial are prior wilful violations of the broker-dealer registration or the anti-fraud provisions of the federal securities statutes, or the making of wilfully false and misleading statements of material facts in the application for registration—all of which the Commission found petitioner to have been guilty. As previously indicated, the Commission concluded that denial of registration was in the public interest.

As an unsuccessful applicant petitioner is entitled to judicial review of the Commission's determination under Section 25 (a) of the 1934 Act, 15 U. S. C. § 78y (a). The statute provides, however, that in such review proceedings "The finding of the Commission as to the facts, if supported by substantial evidence, shall be conclusive." *Ibid.* This serves to emphasize the primary authority and responsibility of the Commission with respect to the registration of persons who seek to do business as securities brokers and dealers, and the more limited authority of the reviewing court to disturb the administrative determination only if the factual findings are not supported by substantial evidence or if the Commission has departed from the law.

Petitioner misconceives the purpose of the statute and the nature of the Commission's responsibility thereunder when he attacks the denial order as an excessive "penalty" for his past derelictions (R. 37, 256; Pet. Br. 37). Whatever the disadvantage to petitioner, the statutory objective is not to inflict punishment on an applicant for past misdeeds

but rather to protect the investing public by excluding undesirable persons from the securities business. See *Wright* v. *SEC*, 112 F. 2d 89, 94 (C. A. 2, 1940).

Petitioner seems to assume also that he has something in the nature of a vested interest in continuing to engage in the securities business in which he admittedly was illegally engaged at the time the Commission sought an injunction. This, of course, is not so. Petitioner has no lawful securities business which is now at stake, but is seeking a license to engage lawfully in that business for the first time. If the public interest requires denial, as the Commission found, petitioner is not deprived of any legal right by the unavailability of a contemplated source of income.

We turn now to the Commission's findings and to the evidence which supports them.

I. For several years prior to the instant application petitioner did business as a securities broker and dealer without registration in wilful violation of Section 15 (a) of the Securities Exchange Act of 1934.

The Commission found, and petitioner here admits (R. 248; Pet. Br. 3), that for several years prior to the instant application petitioner engaged in business as a securities broker and dealer without registration in wilful violation of the statute.

According to the Commission's findings (R. 250.4) in 1951 and 1952 petitioner effected transactions in Las Vegas, Nevada, and in various places in California with various members of the public involving the purchase and sale of stock of the Las Vegas Thoroughbred Racing Association, a corporation formed to construct and operate a horse racing track.

at Las Vegas. Prior thereto he had acted as a salesman for the underwriter of the initial offering of the stock of that association. In 1952 the racing association was reorganized under Chapter X of the Bankruptcy Act. Petitioner then sought—through advertisements placed in newspapers in Los Angeles and Las Vegas—to sell to the public stock of the successor corporation, the Las Vegas Jockey Club.

In 1953 and 1954 petitioner was engaged in selling stock in Golden Nugget, Inc., a corporation operating a casino and restaurant in Las Vegas. He placed advertisements offering the stock for sale in several newspapers, including newspapers in Denver, Salt Lake City, and Las Vegas. He replied by mail to inquiries which resulted from the advertisements. He made arrangements with various banks for handling the transactions, and sold stock to over fifty persons residing in several states.

Petitioner was also engaged during this period in selling stock of Show Boat Hotel, Inc., and Terry Drilling Company, and used the mails and facilities of interstate commerce in offering these securities to the public.

Petitioner does not challenge the Commission's finding that these violations were wilful. The Commission noted, in this connection, that following the close of the offering of stock of the racing association in 1951, petitioner discussed the matter of trading in that stock with Burr, the Commission's Assistant Regional Administrator in charge of its Los Angeles branch office, who advised him to apply for registration as a broker-dealer. Subsequently, in May of

1952, after receiving information that petitioner had been effecting transactions Burr again warned him that he should seek registration and sent him the necessary application forms. Thereafter, on two subsequent occasions Burr again warned petitioner that he was violating the law and should apply for registration. The Commission also took cognizance of the fact that petitioner continued to do business in violation of Section 15 (a) during the period that his first application for registration was pending and after it was withdrawn. As previously indicated, the instant application was filed only after the Commission instituted court action to enjoin petitioner from further violations of the statute.

In a portion of the Hearing Examiner's Recommended Decision which petitioner adopts in his brief (R. 249.39; Pet. Br. 29) petitioner is described as having "displayed a somewhat callous disregard of the consequences of his acts." The Hearing Examiner had no difficulty in concluding, as did the Commission, that the aforementioned violations were clearly wilful.

Since petitioner does not challenge these findings, we shall not labor the point. It should be borne in mind, however, that these continued and deliberate violations were an important factor in the determination below and would in themselves have justified a finding that denial of the application was in the public interest. *Cf. In re Alexander Smith,* 22 S. E. C. 13, 19–20 (1946).

II. Petitioner wilfully violated the anti-fraud provisions of the Securities Act of 1933 and the Securities Exchange Act of 1934 in his dealings with a customer.

The Commission also found (R. 250.5–250.7) that petitioner wilfully violated the anti-fraud provisions of Section 17 (a) of the 1933 Act, Section 10 (b) of the 1934 Act and Rule X–10B–5 thereunder, and Section 15 (c) (1) of the 1934 Act and Rule X–15C1–2 thereunder, in his dealings with a "Mr. H" whose stock he undertook to sell. "Mr. H" is one Earl B. Hayward, of Santa Barbara, California (R. 63).

According to the Commission's findings, in 1951 Hayward purchased from petitioner 3,000 units (consisting of 3,000 shares of preferred stock and 3,000 shares of common stock) of the stock of the Las Vegas Thoroughbred Racing Association during the public offering of those securities when petitioner was a salesman for the underwriter. Hayward paid $5.00 a unit, or a total of $15,000. Subsequently Hayward became dissatisfied with the progress of the construction of the race track and asked petitioner to try to dispose of some of his stock for him, stating that he wanted to get his money back. Petitioner advised him that he could not sell the stock for as much as $5.00 a unit, but thought he could get $3 or $4 a unit. Hayward eventually agreed to the sale of 200 units at $3 a unit, and 800 units at $4 a unit. Some time prior to February 21, 1952, he sent petitioner his certificates for 1,000 units to be sold (R. 250.5).

The Commission found, however, that prior to this arrangement with Hayward, petitioner had been advised by a "Mr. F," one William E. Fox, of South

Gate, California (R. 143), that Fox and some associates desired to invest $12,000 to $15,000 in stock of the racing association. Petitioner, in turn, had advised Fox that the current market price was $6.00 a unit and that he thought he could obtain some units for Fox at that price. When petitioner received Hayward's certificates for 1,000 units, he sold 500 of them to Fox at $6.00 per unit, and had the balance transferred to himself. He wrote Fox explaining that the delay in sending him the units was occasioned by extreme difficulty in obtaining the stock, but that he would try to obtain more if Fox advised him promptly. On February 29, 1952, Fox sent petitioner his check for $3,000 in payment for the 500 units. Thereafter, on March 3, 1952, petitioner sent Hayward a check for $600 which he stated covered the sale of 200 units at $3 a unit. He said that he still held 800 units which he hoped to be able to dispose of shortly at $4.00 per unit (R. 250.6–250.7).

In March of 1952 petitioner sold the remaining 500 units of Hayward's stock to Fox and his associates at $6.00 per unit and received payment therefor; but he did not report any further sales to Hayward until May 14, 1952. He then wrote Hayward that he had sold only 200 additional units at $4.00 per unit for which he enclosed a check for $800 and that he hoped to dispose of the balance of 600 units shortly. The check was dishonored for insufficient funds, and Hayward waited another four months, until September of 1952, before petitioner paid him the $800. Hayward waited nearly two years more before receiving any

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further payments from petitioner. In June of 1954, petitioner paid him $200 and gave him a note for $2,200 for the remaining 600 units (R. 250.6).

The Commission found that Hayward had no independent knowledge and relied entirely on petitioner's representations as to the market value of the stock. It was not contemplated that petitioner would purchase Hayward's stock with his own funds, but rather that he would act for Hayward in selling the stock at what he represented was the best price then obtainable. His representation that he could not obtain $5.00 per unit, but only $3.00 and $4.00, was fraudulent since he knew at that time that Fox and his associates were willing to pay $6.00 per unit. He further violated the statutory anti-fraud provisions in his gross misrepresentations and false accounting to Hayward as respects the disposition of the stock. All of this, the Commission concluded, clearly operated as a fraud and deceit upon Hayward (R. 250.6–250.7).

Petitioner challenges these findings, claiming that he bought Hayward's stock for his own account, that Hayward was satisfied with the $3.00 and $4.00 prices and had no interest whatsoever in what petitioner might obtain for the stock on resale, and that his failure to pay Hayward promptly was due to financial difficulties which he subsequently encountered and involved no fraud or deceit upon Hayward. Petitioner's version was accepted by the Hearing Examiner. As indicated above, however, the Commission found that the evidence negated petitioner's explanation. Under Section 25 (a) of the Act, the Commission's

findings are governing if supported by "substantial evidence."

The evidence as a whole leaves little room for doubt that petitioner undertook to sell Hayward's stock for him at what he falsely represented was the best price he could then obtain. Hayward testified that he "asked [petitioner] if he wouldn't take and sell some of my stock, get my money back" (R. 68). He said he wanted to get at least $5.00 per unit, the price he had paid (R. 99, 100, 101, 106, 115, 122), but was advised by petitioner that the $5.00 price was not obtainable but that he could probably get $3.00 or $4.00 per unit (R. 115, 117, 118, 119, 121, 122, 124). While Hayward prided himself on his knowledge of the construction business and his ability to evaluate the extent of the progress being made in constructing the race track (R. 107–108, 111–112), he testified, "I don't know what the market value of the stock was * * * I don't know anything about stocks" (R. 103–104; see also R. 119). He said that he made no independent inquiry as to the market value of the stock (R. 122), but relied entirely on the petitioner, and that he had "no reason to doubt his integrity up to that point" (R. 119). When petitioner advised him that $5.00 could not be obtained (R. 115, 118, 124) and told him that $3.00 and $4.00 was the best he could get, he said he replied, "If that's all you can get, let's sell it" (R. 117). In light of petitioner's advice, he considered himself "fortunate in being able to recover $3 and $4" for the stock (R. 102–103). He was unequivocal in his testimony that petitioner was to sell the stock for him, and was not

buying it from him (R. 95, 119). While he stated that thereafter he did not feel that it was any of his concern what petitioner actually got for the stock, he explained that he felt that he had committed himself to accepting $3.00 and $4.00, and "my word is my bond" (R. 125). He observed that he did not expect petitioner to be able to sell the units, "but he did sell them, and that was our agreement, and that is what I expected" (*Ibid.*).

Inconsistent with Hayward's testimony is that of the petitioner who stated, "I told him that I would buy the stock from him at the rate of $3 a share, a unit, for 200 units, and $4 a unit for the balance of the 800 units" (R. 211–212). Petitioner's self-serving statement at the hearing, however, is in direct conflict with his own letters to Hayward at the time of the events in question which were introduced into evidence. Thus, in his letter of March 3, 1952, in which he misrepresented that he had only disposed of 200 units at $3.00 apiece, he stated: "I hope to be able to unload the balance for you shortly" (R. 38). In his letter of May 14, 1952, in which he falsely represented that he had disposed of another 200 units at $4.00 apiece, he stated: "I've sold 200 units of your stock * * * I hope to be able to move the balance of your stock very shortly * * * I hope you understand and appreciate what I'm trying to do for you. I sincerely would like to get you out from under as quickly and for as much as I can" (R. 39). This aspect of the evidence, unfortunately, is not considered in the recommended decision of the Hearing Examiner who apparently reached his conclusion

that petitioner had acted as a principal-dealer on the basis of petitioner's testimony which he regarded as "forthright and unambiguous" (R. 249.16) as opposed to that of Hayward which he characterized as "contradictory * * * confusing and indecisive" (R. 249.23). As previously indicated, however, the contemporaneous correspondence, which is of greater probative value, is consistent with Hayward's testimony and wholly inconsistent with that of the petitioner. It appears also that in October of 1952 petitioner admitted to Burr, the Commission's Assistant Regional Administrator, that in his dealings with Hayward he had acted in an agency capacity (R. 139).

The recommended decision of the Hearing Examiner, which petitioner now adopts as his argument (Pet. Br. 6–18), assumes also, and erroneously, that the statutory anti-fraud provisions would not be violated in this case unless petitioner "actively mislead Hayward and acted other than as a principal or dealer" (R. 249.23). The anti-fraud provisions, of course, were violated if petitioner made false and misleading statements of material facts to Hayward in the transactions in question whether he acted as a principal or as an agent; and the record is replete with evidence of such misrepresentation and deceit on petitioner's part.

Thus, as previously shown, in February of 1952, when petitioner undertook to sell Hayward's stock for him, he replied that he could get no more than $3.00 and $4.00 per unit. The record is barren of any indication that petitioner, through negotiations with potential buyers or otherwise, had any basis for

representing that $3.00 and $4.00 were the best prices obtainable at that time. On the contrary, the record shows that he then had purchasers who were ready, willing and able to pay $6.00 a unit and who subsequently bought all of Hayward's stock at that price. William E. Fox, who with some associates had purchased a sizeable block of the stock from petitioner in November of 1951, testified that he and his wife decided to invest $12,000 to $15,000 in stock of the racing association and had left that thought with petitioner (R. 154). In February of 1952 Fox had a long-distance telephone conversation with petitioner concerning further acquisitions in which he indicated that he and his associates were interested in buying more stock at what he assumed to be the current market of $6.00 per unit (R. 158–159). After receipt of Hayward's stock petitioner delivered 500 units to Fox and his associates at $6.00 per unit and then held Fox up another month before he let him and his associates have the remaining 500 units at the $6.00 price (R. 41, 162, 163, 192, 193.)[11] In transmitting the first 500 units to Fox under a covering letter of February 21, 1952, he stated: "I regret the delay, but it has been extremely difficult to acquire the stock * * * I feel that the next few weeks until things are settled will be the only time that I may be able to pick up any further units" (R. 45–46).

[11] There is some suggestion in the record that, unknown to Hayward, petitioner may actually have sold Hayward's stock to Fox and his associates at the $6.00 price even before Hayward finally agreed to take $3.00 and $4.00 as the best prices obtainable. See R. 41, 117, 122–123.

Nearly two weeks later, on March 3, 1952, when petitioner made a partial remittance to Hayward, he falsely represented in his covering letter that he had only been able to sell 200 units at $3.00 a unit (R. 38).

By March 28, 1952, petitioner had sold all of Hayward's 1,000 units and had received a total of $6,000 (R. 136–137, 249.21). Yet, he made no further report to Hayward until the middle of May when he sent him a check in the amount of $800 for 200 additional units. He falsely represented in his covering letter of May 14, 1952, that he had sold these units at $4.00 apiece, and that he still had 600 units of Hayward's stock which he expected to sell shortly. He further stated in that letter: "The race track is now under Bankruptcy Act number 10 and its a bit difficult finding anyone crazy enough to purchase the stock; however, Barnum said, 'There's a new one born every day' " (R. 39).

It appears that the Chapter X petition was filed in January of 1952 (R. 61), and that notwithstanding the pendency of that proceeding Fox and his associates were willing to pay $6.00 per unit which, Fox was satisfied, represented the "going price" (R. 158), that they bought 1,400 units from petitioner at that price in February and March of 1952, including all of Hayward's stock (R. 41, 45, 159, 165–166), and that thereafter, in July and October of 1952, Fox bought additional shares from petitioner at the $6.00 price (R. 167, 168).

The $800 check petitioner sent Hayward in May of 1952 was dishonored, and petitioner did not make it good until September of that year. Thereafter, he

made no payment on the $2,400 balance for nearly two years and made a small partial payment then only after Hayward turned the matter over to a lawyer (R. 87-90), at which time he gave him $200 in cash and a note for the balance (R. 80).

Thus, not only did petitioner misrepresent to Hayward the best price he could obtain for the stock, but continued to misrepresent the amounts which he had sold for him and the prices he had obtained therefor, and was grossly deceitful in his accounting. While the record clearly establishes that petitioner undertook to sell the stock on Hayward's behalf, his misrepresentations and deceit in the transactions in question would have violated the statutory anti-fraud provisions even had he acted as a principal. As previously indicated, this aspect of the case was not dealt with by the Hearing Examiner who apparently assumed, and erroneously so, that the determination of fraud and deceit necessarily turned on proof of a principal and agent relationship.

III. Petitioner's financial statement in his application for registration was wilfully false and misleading in contravention of Section 15 (b) of the Securities Exchange Act of 1934 and Rule X–15B–8 thereunder.

The Commission found also that in contravention of Rule X–15B–8 petitioner had wilfully understated his liabilities in the sworn financial statement which he submitted in his application for registration (R. 250.8–250.9). That rule, promulgated under Section 15 (b), provides that every applicant for registration shall file with his application a statement of financial condition in such detail as will disclose the

nature and amount of his assets and liabilities and his net worth. The rule requires an oath or affirmation that the statement is true and correct.

Petitioner filed and swore to the accuracy of the following statement as of October 26, 1954 (R. 8):

Assets:	
Cash	$3,000.00
House and furniture, 1021 Bracken, Las Vegas	20,000.00
Cadillac automobile	5,500.00
Jewelry and miscellaneous	3,500.00
Showboat Hotel, Inc., stock	2,100.00
Total assets	34,100.00
Liabilities:	
Mortgage on house	9,000.00
Mortgage on car	1,500.00
Miscellaneous	500.00
Total liabilities	11,000.00
Net worth	23,100.00

Petitioner admits that he failed to disclose additional unsecured liabilities in excess of $3,000, including his debt to Hayward (R. 215). He claims the omission was inadvertent. The Commission rejected his proffered explanation and concluded that the omission was wilful (R. 250.9). The Commission referred to the evidence that petitioner had discussed his financial affairs with its Los Angeles branch office before filing the statement, and that he had told Burr, the Commission's representative, that he had settled his account with Hayward and had paid him in full, whereas in fact he owed Hayward $1,900 on the note (R. 250.9, 251.3). Moreover, the Commission considered it "incredible" that the statement of miscellaneous unsecured liabilities at $500 instead of over $3,500 by one who was a sole proprietor without any organ-

ized business could have been a mere "oversight" (R. 251.2). In the Commission's view, the liabilities omitted were substantial and rendered the statement materially false and misleading (R. 250.9).

The Hearing Examiner, whose recommended decision petitioner has adopted as his own argument (Pet. Br. 22–29), agreed that the financial statement was "inadequate" and in need of amendment (R. 249.38). He concluded, however, that there was "insufficient evidence to justify a finding of willfulness" (*Ibid.*). As previously noted, the Commission disagreed.

The Hearing Examiner appears to have been influenced by petitioner's testimony that he had also forgotten to list a leasehold interest which he valued at $10,000 (R. 215, 249.34, 249.35).[12] The lease was one for five years under the Federal Small Tract Act covering five acres near Las Vegas (R. 50). Petitioner testified, and his attorney Dotson stated, that it could be converted into a fee interest at relatively small expense (R. 224–225). Although it could not lawfully be assigned without the approval of the Government, in August of 1953 petitioner sent the lease to Fox as "collateral" for a $1,000 debt (R. 56). The Hearing Examiner found the underlying tract to be worth $7,500 (R. 249.36), and valued the leasehold interest at $5,000 (R. 249.38), an amount greater than the unreported liabilities, which would mean that petitioner's net worth was actually greater than he had

[12] Only a year earlier petitioner had claimed that the property was worth $5,000 (R. 47).

reported.[13] While he did not expressly say so, his finding of "insufficient evidence" of willfulness appears to have been affected by his valuation of the omitted putative asset.

The Commission stated, however, and correctly so, that "The fact that applicant had an unreported putative asset in the form of an interest in real property which may have had a value in excess of the unreported liabilities is irrelevant. The applicable rule calls for disclosure of all liabilities. Insofar as the Hearing Examiner's report may imply that the omission of liabilities may be condoned if there are unreported assets of an equal or greater amount so that the actual net worth of an applicant is greater than that set forth in his sworn statement, the suggestion is specifically disapproved" (R. 251.3).

The record, we believe, amply supports the Commission's finding that the gross understatement of petitioner's unsecured liabilities was wilful. Petitioner was very much aware of these liabilities which were major ones to him, as his correspondence with his customers and their lawyers clearly reveals (R. 46–50, 56–59). As indicated in the Commission's opinion, Burr, the Commission's Assistant Regional Adminis-

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[13] In reaching his valuation the Hearing Examiner relied upon petitioner's self-serving testimony, the unsworn statement of petioner's attorney Dotson, and private conversations with one McCoig, a Las Vegas real estate broker who accompanied the Hearing Examiner on a post-hearing inspection of the tract (R. 249.35–249.36). Apart from the irrelevancy of the valuation in the determination under Rule X–15B–8, Dotson's and McCoig's unsworn statements were clearly without evidentiary value.

trator, had questioned him about his debt to Hayward in connection with his first application for registration (which did not reveal these liabilities), and he had falsely represented that he had settled that obligation and had paid Hayward in full (R. 142). At the time of the instant filing, petitioner was still making installment payments on some of these debts and in fact made a $200 payment to Hayward on the day Hayward testified (R. 109). Considering all of the evidence, the Commission properly rejected as incredible petitioner's contention that his omission to disclose the aforementioned liabilities was not deliberate but a mere oversight.

IV. The Commission properly found that denial of registration was in the public interest.

The record establishes, and the Commission found, that for several years prior to the instant application petitioner had unlawfully done business as a securities broker-dealer in disregard of repeated admonitions by the Commission's staff, that he was guilty of fraudulent misrepresentations and deceit in his dealing with a customer in wilful violation of the statutory anti-fraud provisions, and that the financial statement which he submitted in the instant application was wilfully false and misleading in material respects (R. 250.9). The record shows also that he made false statements to Burr, the Commission's representative, regarding the nature of his activities (R. 139) and his liabilities to Hayward (R. 142). Indicative also of petitioner's disregard of the law was his continued activities as a broker-dealer in deliberate violation of the statute during the period his first

application was pending and after its withdrawal, and the fact that the instant application was filed only after the Commission instituted a court action for an injunction. See pp. 4–5, *supra*. Relevant also is petitioner's lack of an adequate sense of financial responsibility to his customers as is shown by his failure to make timely and proper remittances of the proceeds of the sale of Hayward's stock (see pp. 15–16, 20–22, *supra*), and by the instances in which he gave his customers bad checks (R. 72, 75, 92, 180).[14] In ascertaining the "public interest," it is the character of the particular statutory violations and other improprieties found, rather than the financial consequences, which is of prime importance. *Cf. In re Burley & Co.*, 23 S. E. C. 461, 468–9 (1946); *In re General Securities Corp.*, 18 S. E. C. 635, 637 (1945). We think it clear that the Commission properly concluded that denial of registration in this case was in the public interest (R. 250.9).

The Hearing Examiner's contrary recommendation that the public interest did not require denial of registration appears to have been based in part on the mistaken notion that petitioner's derelictions were confined merely to his prior failure to seek regis-

[14] Of interest also, in this connection, are indications in the record that while petitioner was requiring customers to accept small installment payments on monies due them on a claim of inability to meet his obligations he was accumulating substantial possessions of his own—including cash, real estate, and securities—and maintaining a Cadillac automobile which he valued at $5,500 and on which he appears to have made payments of $1,500 between November 10, 1953, and October 26, 1954 (R. 8, 46–48, 49–50, 56–58, 71, 84, 87, 89, 91–93, 109, 168–170, 173–179, 184–185, 194–197).

tration, which petitioner corrected, in part on his feeling that petitioner had been forthright in his testimony and that he sincerely desired to comply with the law, and in part on his erroneous concept of denial as a personal "penalty" (R. 249.40–249.42). As we have shown, however, petitioner's illegal conduct was of much greater scope and of a character which clearly demonstrated his unfitness to engage in the securities business with the public and to handle other people's accounts. As previously indicated, petitioner's testimony, which the Hearing Examiner regarded as "forthright," conflicted with his own letters written at the time of the events in question—writings upon which the Commission properly relied in ascertaining the facts. Petitioner's statements at the hearing of his earnest desire to comply with the law, it would also appear, are completely overshadowed by the illegal activities in which he deliberately engaged over a period of years and the fact that the instant application was filed only after the Commission went to court. As for the suggestion that petitioner has been punished enough by the cost and duration of these proceedings, and that no "additional penalty" is warranted, we have already pointed out that the purpose of denial of registration is not penal but to protect the investing public by excluding undesirable persons from the securities business.

To our knowledge the record contains nothing which would justify a conclusion contrary to that reached by the Commission.

V. The propriety of the denial order is unaffected by the Commission's disagreement with the findings of the hearing examiner.

Under the statute, it is the Commission which must decide whether an applicant shall be permitted to be registered as a broker-dealer, and which must make the findings necessary to that determination. Section 15 (b) of the 1934 Act. The Act further provides that, upon judicial review of the Commission's order, the Commission's findings of fact shall be conclusive if supported by "substantial evidence." Section 25 (a). Substantial evidence, of course, is more than a "mere scintilla." It is "such relevant evidence as a reasonable mind might accept as adequate to support a conclusion." *Consolidated Edison Co.* v. *NLRB,* 305 U. S. 197, 229 (1938). "* * * it must be enough to justify, if the trial were to a jury, a refusal to direct a verdict when the conclusion sought to be drawn from it is one of fact for the jury." *NLRB* v. *Columbian Enameling & Stamping Co.,* 306 U. S. 292, 300 (1939). See also *Universal Camera Corp.* v. *NLRB,* 340 U. S. 474 (1951). We believe that we have shown that the Commission's findings are clearly supported by such evidence and, moreover, that the record does not justify contrary findings.

Under the Commission's Rules of Practice, Rule IX (d), 17 C. F. R. § 201.9 (d), the recommended decision of a hearing examiner is advisory only and does not bind the Commission. The rule requires that the initial page of every recommended decision shall so state; and, in accordance with that requirement, the recommended decision in this case so stated

(R. 249.1). The Supreme Court has emphasized that the Administrative Procedure Act has not modified in any way the "substantial evidence" rule when an agency and its hearing examiner disagree, *Universal Camera Corp.* v. *NLRB,* 340 U. S. 474 (1951), and has expressly rejected the notion that the "clearly erroneous" rule has any applicability to the findings of a hearing examiner, *FCC* v. *Allentown Broadcasting Corp.,* 349 U. S. 358 (1955). See also *NLRB* v. *Pacific Intermountain Express Co.,* 228 F. 2d 270 (C. A. 8, 1955).

Petitioner's suggestion that the Commission ignored the Hearing Examiner's report is an unwarranted reflection upon the good faith of the Commission when it stated in its opinion on denial of rehearing that—"The fact that our Findings and Opinion did not include a detailed discussion of the recommended findings of the Hearing Examiner should not be construed as an indication that they were not given due attention" (R. 251.2). Petitioner likewise does not, and cannot, proffer any substantiation for his further suggestion that the Commission itself never read the record. Here again the Commission expressly stated in its Findings and Opinion that it had independently reviewed the record (R. 250.4). Moreover, on the petition for rehearing, the Commission took occasion to characterize as completely "unfounded" petitioner's charge that it had no familiarity with the record (R. 251.2).

Nor is there anything to support petitioner's innuendo that the Commission relied upon a digest of

the record prepared by its staff, and that the ultimate decision in this case was made by "junior staff assistants" (Pet. Br. 34–35). Whether or not the Commission had the benefit of a digest of the record prepared by its Opinion Writing Office is, of course, "part of [the] internal decisional process which may not be probed on appeal." *Norris & Hirschberg, Inc.* v. *SEC*, 163 F. 2d 689, 693 (C. A. D. C. 1947). Even had the Commission utilized the services of its subordinates in this fashion there would have been no impropriety. *Ibid.* Petitioner's quotation from *Morgan* v. *U. S.*, 298 U. S. 468, 481 (1936)—"the one who decides must hear"—is not complete. Immediately thereafter the Supreme Court also stated: "This necessary rule does not preclude practicable administrative procedure in obtaining the aid of assistants in the department * * * Evidence may be taken by an examiner. Evidence thus taken may be sifted and analyzed by competent subordinates. * * *."

Petitioner's assertion that "The Commission has not had the benefit of the comments of counsel for Pierce on the 'independent review' on which Pierce's fate rests" (Pet. Br. 35) is singularly lacking in grace. Petitioner's counsel filed a brief in opposition to the exceptions taken by the Division of Trading and Exchanges to the Hearing Examiner's recommended decision (Tr. Doc. 27). In that brief his counsel declined even to discuss the staff's exceptions and arguments, but instead made a broad demand for blanket adoption of the Hearing Examiner's recommended decision without any review whatsoever. Petitioner's counsel did not seek to present oral argument to the Commission whose function they con-

ceived to be simply that of giving effect to the recommendation of the Hearing Examiner favorable to their client. It was only after the Commission handed down its adverse findings and opinion that they sought in a petition for rehearing to present any argument on the merits of the case (R. 22). As previously noted, they requested and obtained from the Commission approximately six weeks instead of the usual five days in which to file that petition. Thereafter, their arguments were fully considered by the Commission and properly found to be wholly lacking in merit (R. 251.3).

CONCLUSION

The Commission properly exercised its statutory function and responsibility in denying petitioner authorization to do business as a securities broker and dealer with members of the investing public. Its findings are fully supported by the record. No showing has been made why this Court should disturb the Commission's determination. The denial order of August 16, 1955, should be affirmed.

Respectfully submitted.

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APPENDIX

Statutes and Rules Involved

Section 15 (a) of the Securities Exchange Act of 1934, 15 U. S. C. § 78*o* (a), provides:

> No broker or dealer (other than one whose business is exclusively intrastate) shall make use of the mails or of any means or instrumentality of interstate commerce to effect any transaction in, or to induce the purchase or sale of, any security (other than an exempted security or commercial paper, bankers' acceptances, or commercial bills) otherwise than on a national securities exchange, unless such broker or dealer is registered in accordance with subsection (b) of this section.

Section 15 (b) of the Securities Exchange Act of 1934, 15 U. S. C. § 78*o* (b), provides in relevant part:

> A broker or dealer may be registered for the purposes of this section by filing with the Commission an application for registration, which shall contain such information in such detail as to such broker or dealer and any person directly or indirectly controlling or controlled by , or under direct or indirect common control with, such broker or dealer, as the Commission may by rules and regulations require as necessary or appropriate in the public interest or for the protection of investors. Except as hereinafter provided, such registration shall become effective thirty days after the receipt of such application by the Commission or within such shorter period of time as the Commission may determine.

* * * * *

> The Commission shall, after appropriate notice and opportunity for hearing, by order deny registration to or revoke the registration of any broker or dealer if it finds that such denial or revocation is in the public interest and that (1) such broker or dealer whether prior or subsequent to becoming such, or (2) any partner, officer, director, or branch manager of such broker or dealer (or any person occupying a similar status or performing similar functions), or any person directly or indirectly controlling or controlled by such broker or dealer, whether prior or subsequent to becoming such, (A) has willfully made or caused to be made in any application for registration pursuant to this subsection or in any document supplemental thereto or in any proceeding before the Commission with respect to registration pursuant to this subsection any statement which was at the time and in the light of the circumstances under which it was made false or misleading with respect to any material fact; or (B) has been convicted within ten years preceding the filing of any such application or at any time thereafter of any felony or misdemeanor involving the purchase or sale of any security or arising out of the conduct of the business of a broker or dealer; or (C) is permanently or temporarily enjoined by order, judgment, or decree of any court of competent jurisdiction from engaging in or continuing any conduct or practice in connection with the purchase or sale of any security; or (D) has willfully violated any provision of the Securities Act of 1933, as amended, or of this title, or of any rule or regulation thereunder. * * *

Section 17 (a) of the Securities Act of 1933, 15 U. S. C. § 77q (a) provides:

> It shall be unlawful for any person in the offer or sale of any securities by the use of any means or instruments of transportation or com-

munication in interstate commerce or by the use of the mails, directly or indirectly—

(1) to employ any device, scheme, or artifice to defraud, or

(2) to obtain money or property by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(3) to engage in any transaction, practice, or course of business which operates or would operate as a fraud or deceit upon the purchaser.

Section 10 (b) of the Securities Exchange Act of 1934, 15 U. S. C. § 78j (b) provides:

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce or of the mails, or of any facility of any national securities exchange—

To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors.

Rule X–10B–5 promulgated under Section 10 (b) of the Securities Exchange Act of 1934, 17 C. F. R. § 240.10b–5, provides:

It shall be unlawful for any person, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails, or of any facility of any national securities exchange,

(1) to employ any device, scheme, or artifice to defraud,

(2) to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in the light of the circumstances under which they were made, not misleading, or

(3) to engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person,

in connection with the purchase or sale of any security.

Section 15 (c) (1) of the Securities Exchange Act of 1934, 15 U. S. C. § 78*o* (c) (1), provides:

> No broker or dealer shall make use of the mails or of any means or instrumentality of interstate commerce to effect any transaction in, or to induce the purchase or sale of, any security (other than commercial paper, bankers' acceptances, or commercial bills) otherwise than on a national securities exchange, by means of any manipulative, deceptive, or other fraudulent device or contrivance. The Commission shall, for the purposes of this subsection, by rules and regulations define such devices or contrivances as are manipulative, deceptive, or otherwise fraudulent.

Rule X–15C1–2 promulgated under Section 15 (c) (1) of the Securities Exchange Act of 1934, 17 C. F. R. § 240.15c1–2, provides in relevant part:

> (a) The term "manipulative, deceptive, or other fraudulent device or contrivance", as used in section 15 (c) (1) of the Act, is hereby defined to include any act, practice, or course of business which operates or would operate as a fraud or deceit upon any person.
>
> (b) The term "manipulative, deceptive, or other fraudulent device or contrivance", as used in section 15 (c) (1) of the Act, is hereby defined to include any untrue statement of a material fact and any omission to state a material fact necessary in order to make the

statements made, in the light of the circumstances under which they are made, not misleading, which statement or omission is made with knowledge or reasonable grounds to believe that it is untrue or misleading.

Rule X–15B–8 promulgated under Section 15 (b) of the Securities Exchange Act of 1934, 17 C. F. R. § 240.15b–8, provides in relevant part:

> (a) Every broker or dealer who files an application for registration on Form BD shall file with such application, in duplicate original, a statement of financial condition in such detail as will disclose the nature and amount of assets and liabilities and the net worth of such broker or dealer (securities of such broker or dealer or in which such broker or dealer has an interest shall be listed in a separate schedule and valued at the market) as of a date within 30 days of the date on which such statement is filed; *provided, however,* that this requirement shall not apply to a partnership succeeding to and continuing the business of another partnership registered as a broker or dealer at the time of such succession. Attached to such statement shall be an oath or affirmation that such statement is true and correct to the best knowledge and belief of the person making such oath or affirmation. The oath or affirmation shall be made before a person duly authorized to administer such oath or affirmation. If the broker or dealer is a sole proprietorship, the oath or affirmation shall be made by the proprietor; if a partnership, by a general partner; if a corporation, by a duly authorized officer.
>
> * * * * *
>
> (c) The statement of financial condition required by this rule shall constitute a "document supplemental" to such application for registration within the meaning of Section 15 (b) of the Act.

Section 25 (a) of the Securities Exchange Act of 1934, 15 U. S. C. § 78y (a), provides in relevant part:

> Any person aggrieved by an order issued by the Commission in a proceeding under this title to which such person is a party may obtain a review of such order in the Circuit Court of Appeals of the United States, within any circuit wherein such person resides or has his principal place of business, or in the Court of Appeals of the District of Columbia, by filing in such court, within sixty days after the entry of such order, a written petition praying that the order of the Commission be modified or set aside in whole or in part. A copy of such petition shall be forthwith served upon any member of the Commission, and thereupon the Commission shall certify and file in the court a transcript of the record upon which the order complained of was entered. Upon the filing of such transcript such court shall have exclusive jurisdiction to affirm, modify, and enforce or set aside such order, in whole or in part. No objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission. The finding of the Commission as to the facts, if supported by substantial evidence, shall be conclusive. * * *

U. S. GOVERNMENT PRINTING OFFICE: 1956